United States Court of Appeals

for the Second Circuit

APPELLEE'S BRIEF

74-2326

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

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In the Matter of	:	In Proceedings for an Arrangement.
D. H. OVERMYER CO., INC. (Florida),	:	
Debtor-Appellant,	:	No. 73 B 1134
-and-	:	
ROBERT P. HERZOG,	:	
Receiver-Appellant,	:	
-and-	:	
ROBERT S. KAHN and DOROTHY H. KAHN,	:	
Appellees.	:	

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BRIEF OF APPELLEES

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STATEMENT

The appellees, whom we represent, previously filed a brief with the Bankruptcy Court and one with the District Court and this brief (pursuant to this Court's order dated October 15, 1974) is submitted as a supplement to the said briefs.

The appellees predicated their right to a return of the property which they had leased to the debtor upon the ground that the lease contained a bankruptcy clause which provided for the termination of the lease in the event of the filing of a petition for arrangement or a bankruptcy petition. The appellants in essence opposed the granting of the application because it would amount to a windfall to the landlords and would be contrary to the equitable jurisdiction of the Court. Both the Bankruptcy Judge and the District Judge in their opinions pointed out that the appellants had failed to present any facts which would warrant the Courts to exercise its equitable jurisdiction and enforced the agreement between the debtor and appellees.

We will show in this memorandum that the appellants completely failed to present any facts justifying the exercise of equitable considerations in favor of the debtor. The appellees unequivocally established that the debtor had been guilty of most inequitable and unfair conduct and that the appellees had

been prejudiced by the debtor's conduct. As a matter of fact, the appellees were able to preserve their property only because of their ability to borrow funds so that the mortgage obligations covering the property in question could be met.

POINT I

THE APPELLANTS FAILED TO PRESENT ANY FACTS WHICH WOULD WARRANT THE COURT FROM FAILING TO ENFORCE THE CLEAR MANDATE OF SECTION 70b, 11 U.S.C. 110. THIS SECTION PROVIDES THAT THE BANKRUPTCY OF A SPECIFIED PARTY WHICH GIVES THE OTHER PARTY AN ELECTION TO TERMINATE A LEASE IS ENFORCIBLE

Despite the tortured argument by the appellants, the law is very clear that a provision in a lease which grants a party an election to terminate in the event of a bankruptcy is enforcible. Bankruptcy Act §70b, 11 U.S.C. 110. The appellants do not claim that the provisions for the termination of a lease in the event of bankruptcy is unclear or doubtful, and thus the provisions of the lease should be enforced. Queens Boulevard Wine and Liquor Corp. v. Blum, et al., F.2d , Docket No. 73-1512 (2d Cir., filed June 11, 1974), the chief reliance of the appellants, does not support the contention of the appellants. All that Queens Boulevard Wine and Liquor Corp. v. Blum, supra, held was that in light of the special circumstances of that case the Court would not terminate the lease. There had been only a minor default, the landlord had security, the debtor's plan

of reorganization been approved by all of the creditors and there was no conduct on the part of the debtor which would warrant the termination of the lease except for a minor dafault. Clearly, in the instant case the appellants failed to present any facts which would warrant the Court to exercise its equitable jurisdiction. The appellants also blithely ignored the wrongful conduct of the debtor which gave rise to this claim and which we will hereafter discuss in this brief.

The appellees purchased the warehouse in question from the debtor and leased the same back to the debtor. The lease provided for a monthly rental of $6,765 together with an escrow for taxes on a monthly basis. The appellees were required to pay interest and amortixation on the first mortgage which in 1973 amounted to a constant monthly payment of $4,473.44, together with taxes of $1,446, or a total payment of $5,919.44. The mortgage provided for interest at the rate of 6-1/2% per annum which obviously in 1973 was a most favorable interest rate and it was essential that the appellees keep this mortgage current and avoid a default thereunder.

Commencing in the latter part of 1972 and the early part of 1973, the debtor began to be delinquent in the payment of rent. As a matter of fact, the debtor failed to pay the March, 1973 rent and the appellees served upon the debtor the

necessary notice required under Florida law demanding that the debtor pay the rent or deliver possession. The debtor refused to do either although it continued to collect the rent from its subtenants. In the stipulation of facts, the debtor conceded that until December of 1973 the monthly rents collected amounted to in excess of $14,300 monthly. In other words, exclusive of minor costs for maintenance and insurance, the debtor realized a gross profit of approximately $6,000 a month but still refused to pay rent to the appellees.

In the action commenced by the appellees in April, 1973, for the recovery of the rent or possession of the property, the debtor resorted to evasive and dilatory tactics to avoid the payment of rent although, as above noted, it was collecting rent far in excess of the rent due to the appellees. The debtor also failed to comply with an order of the Florida Circuit Court, which directed an examination before trial and interposed an ill-founded defense to the effect that the transaction although in form a sale and lease-back consisted of a mortgage transaction. We advert to those facts because they establish that the debtor was thoroughly unprincipled and lacking in integrity. Although it was collecting rents from the leased premises in excess of the lease rent, it made no effort to pay the landlord the amount due under the lease. It is, therefore, with ill-

grace that this debtor, who resorted to all these evasive and unjustified tactics, which certainly deserve condemnation, now requests the Court to exercise its equitable powers in its favor.

Finally, the appellees were successful in entering a judgment against the debtor in the Florida court, for the past due rent which judgment was in excess of $56,000. (Appellees' Exhibit 3 in evidence). During the period the debtor was in default in the payment of rent (although it was effecting rent collections from subtenants) appellees were required to advance to the mortgagee both on account of interest, amortization and for tax escrow the sum of $53,658.81 for the period from May 4 to and including January 4, 1974, plus tax escrow of $3,728.74. (Page 6 of transcript). In other words, to preserve the status of the mortgage and to prevent a foreclosure thereof, the appellees received no return on their investment for a period of almost eight months and were required to borrow during the same period upon their securities a sum in excess of $53,000. Thus, the debtor's conduct resulted in a loss of income to the appellees in excess of $18,000 and an expenditure to prevent foreclosure of the mortgage in the amount of $53,000.

Also, the appellees, in a Florida action, were compelled to move and obtained the appointment of a Receiver of the Rents and Profits since it was inequitable for the debtor to collect rents without paying the rent reserved in the lease to the appellees.

We realize, of course, that the appellants will rationalize that it resorted to all these improper and unwarranted tactics since it was anxious to preserve its interest in the property. However, it is with ill-grace that the debtor can ask this Court of equity to favor it with its discretion and stay the proceedings on the part of the plaintiffs to recover possession of the property where it has been guilty of gross, improper and wrongful conduct causing a serious financial loss and detriment to the appellees.

The appellees have been fortunate in that they were able to borrow upon their securities to be able to make these payments. However, if they had not been able to, the mortgage wpould have been foreclosed and the appellees would have lost their property and their investment.

The foregoing history of the debtor's conduct is clear and convincing proof that the debtor is not entitled to any consideration by a Court of equity to prevent the enforcement of an

obligation which it had assumed. Because the appellees have suffered damage by reason of the conduct of the debtor, the lower Court was fully warranted in refusing to exercise its equitable jurisdiction in favor of the appellants.

POINT II

IN THE ACTION BROUGHT BY THE APPELLEES, IT WAS ESTABLISHED THAT THE DEBTOR COMMITTED ACTS OF DEFAULT UNDER THE LEASE AND THE APPELLEES HAD A CONTRACTUAL RIGHT TO THE LEASED PREMISES

The appellees in this proceeding established that prior to the filing of the proceeding under Chapter XI the debtor had committed the following acts of default, in addition to the filing of a petition for arrangement:

1. The entry of a judgment against the debtor on November 15, 1973 for $56,164.53 which still remains unpaid and of record.

2. The appointment of a Receiver on November 13, 1973 of the rents of said premises.

All of these acts constituted defaults which could not be cured pursuant to the provisions of the lease (Sections 15.01 and 15.03) and accordingly the applicants election to terminate the lease was valid and enforcible. Davidson v. Shivitz, 354 F.2d 946, 949.

This Court stated this rule unequivocally at page 949, supra, as follows:

> "Termination clauses such as those here involved although not looked upon kindly by the courts as a general rule, are valid and enforceable. B.J.M. Realty Corp. v. Ruggiero, 326 F. 2d 281 (2 Cir. 1964)."

Also, it should be noted that in the instant case, the appellees on April 11, 1973, served upon the debtor a notice to pay rent or deliver possession. Thus, the appellees had sought to obtain possession more than six months prior to the filing of the petition herein. It was only because of the dilatory and unjustified defense that the debtor interposed in the Florida proceeding, that the appellees did not recover possession. Also, in the Florida actions, the appellees obtained judgment against the debtor and also had a Receiver appointed, all before the filing of the petition herein.

The debtor prevented the landlord from taking possession by dilatory moves which were wholly unjustified. The forfeiture issue does not exist in this case at all. The issue is will this Court seek to deprive the appellees of their rights to possession which had become fully vested by virtue of the debtor's defaults and which could not be enforced by virtue of the debtor's delaying tactics.

POINT III

THE COURTS BELOW PROPERLY HELD THAT THE PROPOSED PLAN OR ARRANGEMENT WAS UNFEASIBLE

Although in the context of this case, the feasibility of the plan is not really relevant, nevertheless we urge that the Court's determination that the plan was not likely to be adopted was fully justified. The appellants ignore the fact that the Bankruptcy Judge had been in charge of this arrangement proceeding since November of 1973. His determination that the plan had "pie-in-the-sky elements" recognized the reality of the situation and was based upon personal knowledge of the proceedings since the inception thereof. Bankruptcy Judge Roy Babitt has been in charge of this proceeding since its commencement and obviously was relying upon his knowledge of the record of the proceedings to make the determination that the plan could not be effected. No facts were set forth by the debtor to warrant any other conclusion. Indeed, for a period of almost one year, the debtor kept advising the Court, as will appear from the hearings before the Bankruptcy Court, that it hoped to be able to borrow moneys so that it would be in a position to effect a plan. Even at the argument before the District Court, the debtor still contended that it was trying to borrow sufficient funds to be able to effect the plan. This grasping at straws by the

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ROBERT S. KAHN and DOROTHY H. KAHN, :

Appellees. :

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STATE OF NEW YORK, COUNTY OF NEW YORK, ss.:

SYLVIA STUTZEL, being duly sworn, deposes and says, that deponent is not a party to the proceeding, is over 18 years of age and resides at 145 East 16th Street, New York, N.Y.

That on the 5th day of November, 1974, deponent served the within Brief of Appellees upon Levy, Levy & Ruback, Esqs., attorneys for Debtors-Appellants and upon Booth, Lipton & Lipton, Esqs., attorneys for Receiver-Appellant, as follows:

Levy, Levy & Ruback, Esqs.
225 Broadway
New York, New York 10007

Booth, Lipton & Lipton, Esqs.
292 Madison Avenue
New York, New York 10017

The addresses shown are addresses designated by said attorneys for that purpose and deponent deposited a true copy of said Brief of Appelles enclosed in postpaid properly addressed wrappers in an official depository under the exclusive care and custody of the United States post office department within the State of New York.

Sworn to before me this
5th day of November, 1974.

Sylvia R. Stutzel

SOLOMON E. STAR
Notary Public, State of New York
Qualified in Westchester County
No. 60-7155975
Term Expires March 30, 1976

debtor is further proof that the feasibility of the plan is not only remote but impossible of being put through. It thus justified the Bankruptcy Court and the District Court to make their findings as to the impossibility of the plan ever being accepted by the creditors.

CONCLUSION

THE ORDER APPEALED FROM SHOULD BE AFFIRMED IN ALL RESPECTS

Respectfully submitted,

McMANUS & ERNST
Attorneys for Appellees,
Robert S. Kahn and Dorothy H. Kahn

SOLOMON E. STAR,
Of Counsel.

Dated: November 5, 1974.